***Sukuk* – A Brief Introduction**

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Recent modernization in Islamic finance has changed the dynamics of the Islamic financial industry. The demand for *Sukuk* or Islamic securities has become increasingly popular in the last few years and has gained universal acceptance as a feasible alternative to conventional financial products.

Sukuk has developed as one of the most significant mechanisms to raise finance in the market through Islamically-acceptable structures. Aside from the obvious attractiveness to Muslim investors, *Sukuk* may also appeal to conventional investors looking for attractively-priced instruments for regular income and capital gains.

Sukuk, plural of '*Sakk*' means "legal instrument, deed or check". *Sukuk* is the Arabic name for a financial certificate but may also be considered as *Shariah*-compliant 'Bonds'. Although *Sukuk* is generally referred to as Islamic bonds, it is better described as an asset-based investment, as the investor owns an undivided interest in an underlying tangible asset which is proportionate to his investment.

The claim embodied in *Sukuk* is not simply a claim to cash flow but an ownership claim. Monies raised by the issuance of the *Sukuk* notes are used to invest in an underlying asset, a trust is declared over that particular asset and thereby the certificate holder will own a beneficial interest in that asset in proportion to his investment. Therefore, the investor is entitled to the benefits that entail, including a proportion of the return generated by that asset.

There are some similarities between *Sukuk* and conventional bonds. It always has fixed term maturity, bears a coupon (profit) and is tradable on the normal yield price. However, *Sukuk* is structured in such a way that the issuance is not an exchange of paper for money consideration with interest as per conventional bonds. Instead, it is based on an exchange of an approved asset for some financial consideration that allows the investors to earn profits from the said transaction.

Another aspect that differentiates *Sukuk* from conventional bonds from an investor's perspective, is their (*Sukuk*) asset-backed nature. Contrary to the default in the payment of conventional bonds and the investors losing all their wealth, the built-in safety aspect of *Sukuk* being asset-backed reasonably assures the investors of their ability to retrieve a major part of their investment even if things go terribly wrong, since they will be having an undivided share in the ownership of the *Sukuk* assets.

Benefits and Features of *Sukuk*

- Tradable *Shariah*-compliant capital market product providing medium to long term fixed or variable rates of return. *Sukuk* are assessed and rated by rating agencies, which investors use as a guideline to assess risk/ return parameters of a *Sukuk* issue.

- Regular periodic income streams during the investment period with easy and efficient settlement and a possibility of capital appreciation of the *Sukuk*.

- Liquid instruments, tradable in secondary markets.

Types of *Sukuk*

Sukuk can be of many types depending on the type of Islamic modes of financing and trades used in its structuring. The following are the common types of *Sukuk*:

(1) ***Sukuk Ijarah***

This is one of the most common *Sukuk* issuance types, especially for project finance. *Sukuk Ijarah* is a leasing structure coupled with a right available to the lessee to purchase the asset at the end of the lease period. The certificates are issued on stand-alone assets identified on the balance sheet.

The rental rates of return on these *Sukuk* can be fixed or floating depending on the agreement. The cash flow from the lease including rental payments and principle repayments are passed through to investors in the form of coupon and principle payments. The *Sukuk Ijarah* provides an efficient medium-to-long term mode of financing.

(2) ***Sukuk Mudharabah***

This is an agreement made between a party, who provides the capital and another party (an entrepreneur), to enable the entrepreneur to carry out business projects, which will be on a profit sharing basis, according to predetermined ratios agreed on earlier. In the case of losses, the losses are born by the provider of the funds only. *Sukuk Mudharabah* are used to enhance public participation in big investment projects.

(3) ***Sukuk Musharakah***

These are investment *Sukuk* that represent ownership of *Musharakah* equity. The structure of *Musharakah* requires that both parties provide financing to the projects. In case of losses, both parties will lose in proportion to the size of their investment. *Sukuk Musharakah* are used to mobilize funds to establish new projects, or to develop an existing one, or to finance a business activity on the basis of partnership contracts.

(4) ***Sukuk Istisna'***

This type of *Sukuk* has been used for the advance of funding for real estate development, major industrial projects or large items of equipment such as turbines, power plants, ships or aircraft (construction/manufacturing financing).

The Islamic financial institution funds the manufacturer or the contractor during the construction of the asset, acquires title to that asset and up to completion either immediately passes title to the developer on agreed deferred payment terms or, possibly, leases the asset to the developer under *Sukuk Ijarah*.

Conclusion

The *Sukuk* market has grown, both in terms of size and sophistication, fairly rapidly over the last few years. *Sukuk* have confirmed their viability as an alternative means to mobilize medium to long term savings and investments from a huge investor base.